

Office of Chief Counsel
Internal Revenue Service
Memorandum

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date: February 21, 2007

to:

(Large & Mid-Size Business)

from:

(Income Tax & Accounting)

subject: Income Recognition on Sale of Permanent Seat Licenses

This Chief Counsel Advice responds to your request dated November 21, 2006. This advice may not be used or cited as precedent.

LEGEND

Taxpayer =

Stadium =

Date 1 =

Authority =

Team =

Year 1 =

Year 2 =

Year 3 =

Year 4 =

Year 5 =

ISSUES

1. Whether Taxpayer is required to include in income the total sales proceeds from the sale of permanent seat licenses (PSLs) in the first year an agreement is executed, even though payments are received in taxable years.
2. Whether Taxpayer may elect to use the installment sales provisions of § 453 of the Internal Revenue Code if Taxpayer recognizes the total sales proceeds from the sale of the PSLs in the first taxable year.

CONCLUSIONS

1. Taxpayer recognizes income from the sale of PSLs when each installment payment becomes due and payable or each installment payment is received, whichever happens first.
2. Because Taxpayer does not recognize the total sales proceeds in the first year the agreement is executed, § 453 does not apply.

FACTS

On Date 1, Authority licensed Taxpayer as its agent to sell PSLs to Team games to be played at Stadium, . Taxpayer began marketing PSLs and received some applications and initial payments in Year 1,

The terms of the PSL sales are provided in PSL Agreements. Taxpayer executed PSL Agreements for Year 2, Year 3, and Year 4. The PSL Agreements provided that the purchase price of a PSL was payable in installments. The first payment was due at the time the PSL was executed. The remaining installments usually were due in each of the following years. The Agreements granted the purchaser the right to buy season tickets for designated seats at Team's games at Stadium as long as Stadium was Team's home field. This right was not evidenced by any other document (for example, no certificate was issued). Rather, Taxpayer maintained a list of PSL purchasers who had rights to seats under a PSL Agreement.

The PSL Agreements provided for a _____ that required the purchaser to: 1) pay the required deposit; 2) pay the remaining installments due in each of the next _____ succeeding years; and 3) return the signed agreement within _____ days. _____ of the PSL Agreements provided that the purchaser would receive a PSL in consideration of the purchaser: 1) paying the required deposit; 2) promising to pay the next _____ installments; and 3) returning the signed agreement within _____ days.

_____, Taxpayer may withhold tickets and/or terminate the rights of the licensee. These terms constituted Taxpayer's sole recourse if a purchaser failed to make a payment when due or otherwise defaulted. The Agreements included no specific provisions granting Taxpayer the right to collect a missed payment. The default provisions applied to a purchaser's failure to pay amounts due for tickets as well as for the PSL.

LAW AND ANALYSIS

Section 451(a) of the Internal Revenue Code provides that the amount of any item of gross income is included in gross income for the taxable year in which received by the taxpayer, unless under the method of accounting used in computing taxable income, the amount is to be properly accounted for as of a different period. Section 1.451-1(a) of the Income Tax Regulations provides that under an accrual method of accounting, income is includible in gross income when all the events have occurred that fix the right to receive the income and the amount can be determined with reasonable accuracy.

All the events that fix the right to receive income under an accrual method of accounting occur when: (1) the required performance occurs; (2) payment is due; or (3) payment is made, whichever happens first. See Rev. Rul. 2003-10, 2003-1 C.B. 288; Rev. Rul. 2004-52, 2004-1 C.B. 973. See also Schlude v. Commissioner, 372 U.S. 128 (1963).

We assume as a factual matter that Taxpayer received payment from the sale of PSLs in each of _____ succeeding taxable years, beginning with the year a purchaser signed an Agreement (or, in Year 1, when a purchaser signed an application and made an initial payment). The terms of the PSL contracts and the parties' actions are relevant in determining when the payments were due and when Taxpayer's performance occurred. We conclude that the _____ installments were not due and payable until the year and date established under the PSL Agreements, generally the _____ succeeding

years after the purchaser signed an Agreement. Under the terms, Taxpayer had no right to enforce payment of the installments or accelerate the due date for payment. If a purchaser failed to make the payments as required, Taxpayer's recourse was to terminate the purchaser's rights under the contract, including withholding tickets. Therefore, Taxpayer had no fixed, unqualified right to a payment until the due date occurred. See Schlude v. Commissioner; Commissioner of Internal Revenue v. Union Pac. R. Co., 86 F.2d 637 (2nd Cir. 1936); Lucas v. North Texas Lumber Co., 281 U.S. 11 (1930).

We conclude that Taxpayer's performance under the contract occurs when all payments are made. Under the PSL Agreements' a PSL is only when all installments are paid. Additionally, under the default provisions, Taxpayer may deny the purchaser the right to purchase tickets until all required payments are made. Therefore, the purchaser has no right to, and does not receive, a PSL until all payments are made.

Taxpayer has no right to enforce payment of the installments in the year an Agreement is signed by a licensee/purchaser, and the payments are not due and payable until the years of the agreement. Under the terms and conditions of the PSL contracts, the purchaser does not have the right to a PSL until all payments are made under the Agreement, and Taxpayer's performance does not occur until that time. As the performance requirement is not met until the final installment is paid, we conclude that Taxpayer must properly accrue income as each installment is due and payable, or payment is made, whichever occurs first.

As Taxpayer does not recognize the total sales proceeds in the first year the agreement is executed, § 453 does not apply.

We note that the contingencies provided in the PSL Agreement (

) would not prevent Taxpayer from accruing the income if the all events test were otherwise satisfied. When applying the all events test, courts have distinguished between conditions precedent, which must occur before the right to income arises, and conditions subsequent, the occurrence of which will terminate an existing right to income, but which do not preclude accrual of income. Charles Schwab Corp. & Subs. v. Commissioner, 107 T.C. 282, 293 (1996), aff'd, 161 F.3d 1231 (9th Cir. 1998). The contingencies specified are remote and do not constitute a condition precedent to Taxpayer recognizing income.

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Please call (202) 622-7900 if you have any further questions.